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11<sup>th</sup> February 2010

Dear Nicholas

### **Consultation on WPD modification proposal 016 to introduce changes to its EHV charging methodology**

The Renewable Energy Association, having been fully engaged with the structure of distribution charges project for several years, submits its comments on the changes that WPD propose to their EHV methodology to come into effect from 1<sup>st</sup> April 2010. As you are aware our members work on all types of renewable power and heat projects and we have long held the view that cost reflective prices for using the distribution network is key to attracting well located renewable generation projects and avoiding pressure for uneconomic private wire networks in situations where a perfectly good distribution network already exists.

#### **Relationship between this change proposal and the development of common ehv charging methodologies**

We are going to start be answering your question on the relationship between these change proposals and the development of the ehv common distribution charging methodologies and in particular which of the changes proposed here should be incorporated into those methodologies and how much this methodology may have to change in 2011 to line up with one of those methodologies. In this context it is clearly specifically the LRIC methodology that is relevant.

Our view is that it is too early either to be able to say that any of the changes proposed here have general applicability in the common LRIC methodology to apply from April 2011 or to judge how much the WPD methodology, with or

without the proposed changes, may have to change again in 2011 in order to fit in with the common LRIC methodology. We assume that WPD is fully engaged in the process of developing the common methodologies (and the LRIC option in particular) and so the changes that it proposes here will be fully debated in that context, irrespective of whether they are accepted now.

Our conclusion from this which has general applicability to all DNO 2010/2011 ehv tariffs is that they should change as little as possible this year to avoid the possibility of two consecutive years of disruption.

### **Charging of pre April 2005 connected generators**

This is the first substantive issue that you ask for views on and covers WPD's first two change proposals (introducing the charges and making arrangements to provide some compensation for those that have paid deep entry charges).

We remain opposed to levying DUoS charges on pre April 2005 connected generation. Leaving aside the issue of whether DNOs can legally apply charges to many pre 2005 connected generators, the conditions under which generators that connected at that time were well known to and agreed by all concerned parties. Generators paid the full cost of any reinforcements required to accommodate them including the capitalised value of ongoing operation and maintenance of those assets. Where no reinforcement was required in many cases the generator deferred the need for reinforcement but was given no credit for this. There was a clear understanding that no further network related charges would be payable.

#### The position when these parties connected

In case anybody needs reminding of the position pre April 2005 it is instructive to quote from some contemporary material. Firstly we will examine the government sponsored "Technical Guide for the connection of embedded generators to the Distribution Network produced by Econnect and Ilex and published in November 1998.

Section 5.2 covers the "Basis of PES connection charges". Section 5.2.1 starts "In cases where work has to be done to modify an existing connection or to provide an entirely new one, some or all of this work will be done by the PES. Thus, some initial costs will be incurred. These costs are invariably charges to the developer up-front, as part of the connection charge. The PES will also incur costs associated with the operation, maintenance repair and replacement (2010 underlining) of the new or modified connection infrastructure. These operation and maintenance (O&M) costs must be considered in addition to the initial costs. O&M costs are often capitalised and charged to the developer up-front as part of the connection charge."

Section 5.3.1 states “although electricity demand customers pay both connection and use-of-system charges, embedded generators are exempt from the need to pay distribution use-of –system charges. This is because all the PES’s costs associated with generator connections are recovered through the up-front connection charge together with any ongoing service charges.”

We now look at your own December 2000 Structure of Electricity Distribution Charges Initial Consultation Paper. Section 4.26 states:

“Embedded generators presently pay the full capital cost of connection to the local distribution system, including the costs of reinforcement across the system. They do not pay use of system charges on their exports. A number of embedded generators have suggested that these arrangements do not reflect the benefits that embedded generators bring to the distribution network.”

#### The fundamental injustice of imposing charges now

There is a feeling that if somebody has paid deep connection charges they are somehow made whole if those charges are refunded in some way and they are made to pay Use of System charges. That is like saying that if somebody bought a house twenty years ago (say) they would be made whole by confiscating the house, making them pay rent for it and giving them back what they originally paid for it. Note that even if they actually paid nothing for it because twenty years ago nobody else wanted it the same logic would apply, which is analogous to those generators that connected under a deep charging regime but did not have to pay any charges (because no work was required).

The above method of making somebody whole is clearly flawed. What is needed would be to pay somebody the value of their existing position not an amount relating to its cost. The value of the position of somebody who connected pre April 2005 is the fact that for whatever they paid they had certainty of continued access to the network into the future without being effected by any variation in network tariffs. In order to compensate parties properly for the loss of this position one would therefore have to pay them the value of future DUoS payments, which would cancel out having to make these payments and make them whole. It is obviously simpler not to charge them DUoS in the first place.

#### The proposed method of compensating parties who paid deep connection charges

Leaving aside the basic injustice of levying DUoS charges on these generators and the philosophical issue of whether if DUoS charges are imposed the appropriate compensation would relate to the money paid or the value of the existing connection, the method that WPD propose to compensate generators is flawed in that it does not even necessarily compensate them for all the reinforcement that they may have paid for.

Footnote 17 of the consultation states "As mentioned above, there are two site-specific customers connected to WPD's network that have assets that were reinforced pre-2005. However, LRIC charges are calculated by looking at branches. The assets associated with one of these customers are not taken into account when calculating a LRIC branch charge and so there is no impact on that customer's overall charge".

The reinforcement to the assets for the one customer "that are not taken into account when calculating a LRIC branch charge" may or may not have been paid for originally by that customer. One could envisage for example the upgrading of switchgear that would have been paid for by a generator but may not form a part of LRIC branch charges. Thus in the methodology employed the possibility exists of not even giving a generator credit for charges that it actually paid (because the cost does not relate to something that is evaluated in the LRIC methodology). It is therefore in principle inadequate as a methodology even to provide compensation for costs actually paid.

#### Summary on pre April 2005 connected generators

We do not believe that the proposal to impose DUoS charges on pre April 2005 connected generators is more cost reflective than the current arrangements or better facilitates competition in generation. Maintaining the current arrangements would no more be discriminatory than allowing people who had bought a house to keep it without having to pay rent, even though all new parties had to rent their housing.

The arrangements proposed for compensating parties who would become liable for DUoS charges are inadequate in that in principle they may not even refund them some of the charges that they might have paid for. In any event compensation should be for the loss of value of your current position, not what you might have paid for it.

#### **Capping to prevent perceived excessive LRIC charges in some circumstances**

The issue here is complex and goes to the heart of the LRIC methodology, particularly where assets are highly utilised, often because parties have sized generators particularly to take advantage of the precise amount of capacity that is spare. It illustrates the difference between a deep reinforcement connection charging methodology, which recognises the importance of the "lumpiness" of electricity network investments and incremental approaches that are "based" on assumptions about reinforcement cost characteristics being continuous in nature or at least that it is possible to evaluate the cost of bringing an investment forward on the basis of continuous underlying load growth.

We think that enough questions have been raised about the capping methodology to warrant more time to consider it and understand more fully how

the need to cap arises in the first place. We would therefore suggest that providing the combination of approval or not of the other proposed modifications is such that no party would be exposed to "perceived excessive LRIC charges", the capping proposed not be adopted but further work be undertaken as part of the common ehv charging methodology development process to understand how these charges arise and consider the possible alternative ways of capping them. If however what is decided on the other proposed modifications would result in parties being exposed to excessive charges then the capping should be applied as proposed in the knowledge that a different methodology may be utilised from April 2011.

### **Updating the cost of capital**

The proposal to align the cost of capital with that agreed for the next price control period seems sensible.

### **Split of ehv / hv / lv revenue and scaling of generator charges**

We do not understand why the split of revenue between the ehv and the hv/lv pots cannot continue to be assessed on a DNO specific basis and continuing to do so would appear to be the more cost reflective option. If this is significant for WPD with some lv overhead lines one would expect the issue to be much more significant for the EDF (London) area with (untypically) virtually no overhead lines below the 132kv level. We therefore do not understand why the revenue split between different voltage levels should not be done on an actual basis for each DNO without undermining the commonality of the methodologies.

We agree with not scaling the generator charges, both for economic reasons and because of the reasons that you have given for wanting minimum change this year in view of the adoption of a common methodology in 2011.

### **Removal of 10% cap on generator charges**

Providing the use of a one revenue pot approach means that the 10% cap on changes is no longer required (because year to year changes of more than that magnitude become very rare and well justified if they do occur) then we would agree with its removal.

### **Updated references to license conditions and the DCUSA**

We agree with the aim of deleting material from the methodology that is duplicated in the DCUSA.

### **Presentation**

Whilst it is useful to see the effect on the charges of the various changes proposed it could be said to be misleading for actual charges for 2009 / 2010 to

be shown for pre April 2005 connected generators when they were not in fact subject to those charges.

Please let me know if you would like to discuss any of these comments further.

Many thanks,

Gaynor Hartnell

Director of Policy, REA.